

INQUIRY INTO THE PROCUREMENT OF
AUTOMOTIVE SPARE PARTS BY
THE UNITED STATES
GOVERNMENT

FIFTEENTH INTERMEDIATE REPORT
OF THE
COMMITTEE ON EXPENDITURES IN THE
EXECUTIVE DEPARTMENTS



APRIL 25, 1952.—Committed to the Committee of the Whole House
on the State of the Union and ordered to be printed

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LETTER OF TRANSMITTAL

HOUSE OF REPRESENTATIVES,
Washington, D. C., April 25, 1952.

HON. SAM RAYBURN,
Speaker of the House of Representatives,
Washington, D. C.

DEAR MR. SPEAKER: By direction of the Committee on Expenditures in the Executive Departments, I submit herewith the fifteenth intermediate report of its subcommittee.

WILLIAM L. DAWSON, *Chairman:*

III

LETTER OF THE PRESIDENT

Washington, D. C., May 20, 1963

Dear Mr. [Name]:

I am pleased to hear of the [Name]

Washington, D. C.

It is a pleasure to know that the [Name] is the [Name] of the [Name] and that the [Name] is the [Name] of the [Name]. I submit to you the [Name] of the [Name] and the [Name] of the [Name].

Very truly yours,

[Name]

Union Calendar No. 568

82D CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
No. 1811

INQUIRY INTO THE PROCUREMENT OF AUTOMOTIVE SPARE PARTS BY THE UNITED STATES GOVERNMENT

APRIL 25, 1952 — Committed to the Committee of the Whole House on the State
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Mr. DAWSON, from the Committee on Expenditures in the Executive
Departments, submitted the following

FIFTEENTH INTERMEDIATE REPORT

On April 23, 1952, the members of the Committee on Expenditures in the Executive Departments agreed to the report of the Government Operations Subcommittee on inquiry into the procurement of automotive spare parts by the United States Government.

The chairman was directed to transmit a copy to the Speaker of the House.

INTRODUCTION

In the fall of 1950 the General Accounting Office brought to the attention of this subcommittee certain facts which indicated the possibility that the Government was paying excessive prices for automotive parts. Several specific cases had been found where parts had been procured, after competitive bidding, from a vehicle assembler rather than from the company manufacturing the part. One of these cases which the General Accounting Office referred to as typifying a practice more or less general throughout the industry involved the following circumstances:

The Government advertised for 1,000 generators of a certain type; of the bids submitted two were significant—one from Chrysler Motors Inc., for \$77.20 each, and one from Electric Auto-Lite for \$87 each; investigation disclosed that the generator was in fact made by Electric Auto-Lite and had been previously sold to Chrysler for \$52 each.

This case posed several obvious problems which the subcommittee decided should be the subject of intensive study. First, why should Electric Auto-Lite submit a higher bid than a company to which it had sold the part; next, was this case typical of a general trade practice; if so, what were the underlying reasons for the existence of such a practice; what benefits or advantages was the Government receiving for the higher prices being paid for parts when procured indirectly

from vehicle assemblers; and, finally, were any benefits derived worth the added cost? Quite naturally the search for answers to these more obvious questions led to many more which, though not so obvious, were equally as difficult to resolve.

The same field had been explored in 1944 by the Special Senate Committee Investigating the National Defense Program under the chairmanship of Senator James M. Mead (formerly known as the Truman committee). The hearings held at that time contained ample evidence that the situation involved in the Chrysler-Auto-Lite case was not an isolated one; there seemed little doubt but that it was a rather widespread industry practice for parts manufacturers to permit their customers, the vehicle assemblers, to enjoy the replacement-parts business. It was established also that such a practice had existed for some time. Brig. Gen. Walter P. Boatwright, then commanding officer, Chief of Ordnance, Detroit, testified as follows:

Reliance upon vehicle manufacturers for spare parts to service vehicles produced by them has been fundamental War Department policy from the commencement of motorization of the Army in April 1916 up to the present time. Over the years there has been a gradual lessening of this reliance upon vehicle manufacturers, and it is less significant today than at any prior time. For the past 7 months, April to October, inclusive, 1944, 59 percent in dollar volume of the replenishment spare parts were purchased from unit manufacturers, and it is estimated that of the 41 percent purchased from vehicle manufacturers, approximately one-half were parts peculiar to such vehicle manufacturers.

Other historical background was found in a report issued by the Federal Trade Commission in 1939 after a long and detailed study of the entire automobile industry. This report pointed up the extremely profitable nature of the parts business and the fact, later to be confirmed by the subcommittee's own study, that vehicle assemblers relied on the profits from the replacement-parts business to carry them through periods when they might even lose money in the manufacture of the vehicle itself. For example, it was reported that during the 9 years, 1929 to 1937, Ford Motor Co. netted a loss of \$13,085,000 on motor-vehicle sales, but had a profit of \$49,194,000 on parts and accessories. Also, over 6 years of the same period the motor car divisions of General Motors Corp. made an average net profit of 24.85 cents on every dollar of accessories and parts sales as contrasted to 7.18 cents on every dollar of sales of new cars. For Chrysler Corp. the figures were 17.3 on every dollar of parts and accessories sales and 6.6 cents on every dollar of new car sales. See page 1062 of report on motor-vehicle industry (H. Doc. No. 468, 76th Cong., 1st sess.).

The staff study began by selecting from the stock records at the Ordnance Tank-Automotive Center (OTAC) 300 items of automotive parts. These items were selected at random from those which were being procured most frequently during the fiscal years 1949 and 1950. The plan of operation was to break down each procurement of these parts to ascertain (1) who made the part; (2) what did it cost to manufacture; (3) who sold it to the Government and for how much; and (4) what was the nature of the seller's business, that is, was he the basic manufacturer of the part, a distributor, an assembler, or a parts dealer.

Staff representatives obtained information in direct contacts with the following companies:

General Motors Corp., Detroit, Mich.
Chrysler Corp., Detroit, Mich.
Willys Overland Motors, Inc., Toledo, Ohio.
Federal Motor Truck Co., Detroit, Mich.
Timken-Detroit Axle Co., Detroit, Mich.
Spicer Manufacturing Corp. Division, Dana Corp., Toledo, Ohio;
Electric Auto-Lite Co., Toledo, Ohio.
Detroit Harvester Co., Detroit, Mich.
P. L. Grissom & Son, Inc., Detroit, Mich.
Jefferson Chevrolet Co., Inc., Detroit, Mich.
Sid's Auto Truck, Detroit, Mich.
Metro Engineering & Manufacturing Co., Detroit, Mich.
Chelsea Products, Inc., Chelsea, Mich.
Studebaker Corp., South Bend, Ind.

Additionally, the chairman of the subcommittee sent out a questionnaire (exhibit I) requesting certain information and the following companies responded:

Active Gear Co., Inc., Chicago, Ill.
Bendix Westinghouse Automatic Air Brake Co., Elyria, Ohio.
Blackstone Corp., Jamestown, N. Y.
Blood Bros. Machine Co., Allegan, Mich.
Braden Winch Co., Tulsa, Okla.
Carter Carburetor, St. Louis, Mo.
Clark Equipment Co., Buchanan, Mich.
The Crescent Co., Inc., Pawtucket, R. I.
Detroit Aluminum & Brass Co., Detroit, Mich.
Eaton Manufacturing Co., Cleveland, Ohio.
Fairfield Engineering Co., Detroit, Mich.
Federal Mogul Division, Detroit, Mich.
The General Industries Co., Elyria, Ohio.
The H. & O. Manufacturing Co., New Haven, Conn.
Hercules Motor Co., Canton, Ohio.
Industrial Facilities Co., Pontiac, Mich.
Kelsey-Hayes Wheel Co., Detroit, Mich.
Lamson & Sessions Co., Cleveland, Ohio.
Lipe Rollway Corp., Syracuse, N. Y.
Long Manufacturing Division, Borg-Warner Corp., Detroit, Mich.
Maremont Auto Products, Inc., Chicago, Ill.
Midland Steel Co., Detroit, Mich.
Machine Tool & Die Co., Detroit, Mich.
New Process Gear Corp., Syracuse, N. Y.
Pierce Governor Co., Anderson, Ind.
Ross Gear & Tool Co., Lafayette, Ind.
S. A. Shenk & Co., Columbus, Ohio.
Tropic Aire, Inc., Chicago, Ill.
Tobe Deutschmann Corp., Norwood, Mass.
Trico Products Corp., Buffalo, N. Y.
Troy Sunshade Co., Troy, Ohio.
Universal Products Co.

Wagner Electric Corp., St. Louis, Mo.

Warner Electric Brake & Clutch Co., Beloit, Wis.

Warner Gear Corp., Muncie, Ind.

Wayne Foundry & Stamping Co., Detroit, Mich.

Zenith Carburetor Division, Bendix Aviation Corp., Detroit, Mich.

Admittedly, 300 items represented but a very small segment of the total number of parts purchased annually by the Ordnance Corps, through the Tank-Automotive Center (OTAC) in Detroit, as the buying agency for all the military services. Also, the companies involved are by no means the only ones doing this type business with the Government. However, it is believed that the study was sufficiently broad and thorough to bring to light general procurement methods and trade practices in the automotive-parts field.

During the course of the study the subcommittee obtained information indicating the existence of certain improper relationships between high-ranking Government officials and representatives of companies selling automotive parts and other items to the Government. Among the individuals involved in these cases was the commanding officer of the Detroit Arsenal, Brig. Gen. David J. Crawford, and the commanding officer of the Rossford Arsenal, Col. Shirley W. McIlwain. These matters required immediate attention and, accordingly, the Secretary of the Army was called upon by the subcommittee to review the facts developed and take appropriate administrative action. The subcommittee received splendid cooperation from the Department of the Army and wishes to commend Secretary Frank Pace, Jr., for his prompt and forthright handling of these cases. However, the details of these irregularities will not be discussed in this report. While their importance must not be underestimated—for even the soundest of buying policies and procedures will fail if not properly and impartially administered—their connection with the procurement of automotive parts is merely coincidental.

The staff study was carried on in close cooperation with officials of the Ordnance Corps of the Department of the Army, both in Detroit and in Washington. Procedural and administrative deficiencies were immediately brought to the attention of cognizant officials within the Department; in this way many inefficiencies were corrected, even prior to the first hearing held by the subcommittee, which took place on June 25, 1951.

On July 16, 1951, the Chief of Ordnance issued an amendment to existing procurement instructions, the effect of which was to require the reporting by field personnel to the Office of the Chief of Ordnance of certain cases indicating the existence of trade practices resulting in higher cost to the Government. Specific mention was made of cases where the manufacturer of the item has refused to bid or where his bid is in excess of that submitted by his distributors. Also covered by this amendment to the procurement instructions were "other instances where the bidding indicates direct possibility of pyramiding of profits."

On August 17, 1951, the Chief of Ordnance issued a directive to the commanding officers of all ordnance installations covering the subject, Procurement of Replacement Spare Parts. In this directive there was laid down the principle that the procurement of replacement spare parts should wherever practicable be made direct from a

source manufacturing the required complete part or assembly. It was also stated that in such procurement, particularly when large quantities are involved, the Government should receive a price equal to or less than the price quoted by the unit manufacturer to other customers. The directive also stressed the necessity for maintaining a thorough and aggressive cost-analysis procedure, accompanied by a cost consciousness on the part of procurement and management personnel. Then, on August 27, 1951, the Chief of Ordnance instructed contracting officers to stop immediately all action on procurements whenever it appeared that the trade practices referred to in the instructions of July 16, 1951, were involved, and to contact the manufacturers of the particular item to determine whether they would be willing to negotiate a lower price. The contracting officers were further instructed to reject all bids if a lower price could be secured through negotiation.

The facts developed by the staff were summarized in a memorandum which was made available to Ordnance officials and which formed the basis for the final series of hearings held in Detroit the week of December 10, 1951. This memorandum did not purport to arrive at conclusions on the issues; its sole purpose was to present the factual situation as the staff found it.

REPLACEMENT PARTS

Ordnance officials readily conceded that a substantial portion of the purchase of automotive replacement parts is made from the vehicle assembler rather than directly from the basic manufacturer. The precise percentage of procurements made in this indirect manner is difficult to fix with precision, but a recent study made by the Ordnance Corps itself discloses that during the fiscal year 1951 approximately 30 percent of the procurement of parts was made indirectly. Fundamentally, the Department of the Army takes the position that there is no sound basis for procuring replacement parts other than directly from the basic manufacturer, but that the existence of industry practices renders the different procurement officials powerless to buy directly from the source.

The subcommittee found that the automobile industry does have certain well established trade practices with respect to permitting vehicle assemblers to enjoy the replacement-parts business and that these practices have been unnecessarily adding millions to the Government's cost of automotive replacement parts. The case studies presented in a staff memorandum during the hearings contained ample evidence of the manner in which these practices result in excessive prices being charged for the parts. While it does not seem necessary for the purposes of this report to discuss this evidence in detail, perhaps it would be well to refer to several items to illustrate some of the patterns that exist.

In connection with the procurement of an automobile heater made by Tropic-Aire, Inc., 10 invitations to bid were extended, but only 1 bid was received—that from Chrysler Corp. The Government purchased the heater from Chrysler Corp. for \$51.95. In response to a questionnaire submitted to it by the subcommittee, Tropic-Aire represented their manufacturing cost for this heater, including labor and material but excluding administrative expense, to be \$23.244

consisting of \$22.61 basic cost and \$0.634 packaging cost. Chrysler Corp. stated that its costs in connection with the sale of this heater to the Government were:

Price paid Tropic-Aire.....	\$33. 74
Estimated pack, packaging, and shipping.....	9. 50
Estimated procurement, handling, warehousing, and administrative expenses.....	4. 66
Excise tax, at 5 percent of sales price.....	2. 60
Total.....	50. 50
Sales price to Government.....	51. 95
Estimated profit.....	1. 45
Percentage of sales.....	2. 7

Bearing in mind that Chrysler adds nothing to the heater but Government packaging, it is difficult to perceive what possible advantage the Government secures in procuring this type of item from other than the company that manufactures it. The packaging performed in this instance by Tropic-Aire was, of course, a complete economic waste, as it had to be repackaged according to Government specifications by Chrysler. In fact, it well could be considered that all the expense incurred by Chrysler in connection with the handling of this part, except the cost of Government packaging, constituted economic waste. The industry maintains that the Government receives the benefit of expert inspection by the vehicle assembler, but actually the Government's own inspectors are charged with full responsibility for inspection. They neither are permitted, nor should they be permitted, to rely for their determination in this regard upon an inspection made by an employee of the company furnishing the item to the Government.

Another reason frequently put forth as rendering the unit manufacturer unable to deal directly with the Government is the lack of packaging facilities. However, it was brought out before the subcommittee that during the last war most of the unit manufacturers did their own packaging, that most of these companies could do the packaging if they so desired, and that there are packaging firms available—in fact, such firms are many times used by the assemblers themselves. It was brought out, also, that from the standpoint of the Government it is perhaps better to have the packaging done at the source, than to have the item repackaged later, either in the assembler's plant or in a Government depot.

In another case the Government undertook to procure a cylinder head made by the Studebaker Corp. Fifty-five invitations to bid were extended, and only one bid was received, that from P. L. Grissom & Son, Inc., Detroit, Mich., a retail Chevrolet dealer. The part was purchased by the Government from Grissom for \$18.35. According to information received from Studebaker, its manufacturing cost was \$4.04. In tracing the history of this part, it appeared that it was sold by Studebaker to a retail Studebaker dealer, Greenfield Sales & Service, Centerline, Mich., for \$8.10, who sold it to United Auto Electric for \$9.50, who in turn sold it to Grissom for \$12.38. The item as it left Studebaker was exactly the same, except for Government packaging, as when it was received by the Government. In other words, no one in this chain of sales added to the physical

characteristics of the item, but each, of course, added into its own selling price such elements as freight, administrative cost, and profit.

Diamond T is a truck manufacturer, and its president, Mr. Earl J. Bush, frankly admitted that his company needed the replacement-parts business to operate successfully. He stated that the manufacture of trucks is a highly competitive industry and that many companies had failed to survive during the past 30 years. It is the practice of his company to secure parts regularly from certain manufacturers. It is their custom, he stated, to inform themselves before undertaking to do business with a company as to the practice of that company with respect to the replacement-parts business. In other words, he was candid enough to say that unless a parts-manufacturing company permitted its customers, the vehicle assemblers, to enjoy the replacement-parts business without competition from the basic manufacturer, Diamond T would find some other company that would follow that practice.

One of the suppliers of Diamond T is Clark Equipment Co. of Buchanan, Mich. In connection with the sale of one of the parts manufactured by Clark Equipment Co., the Government paid Diamond T \$351.08 for a part which originally had been manufactured by Clark at a cost of \$175.93.

Reference has been made to the fact that in some instances the parts manufacturer was found to be submitting higher bids than the assembler to whom he sold the parts. On one item Hercules Motors Corp. sold a part to Federal Motor Truck Corp. for \$38.78, for which Hercules had a manufacturing cost of \$26.60. The part was sold to the Government for \$46.73 after competitive bidding in which Hercules submitted a bid of \$81.44.

At the hearing a representative of Hercules testified that his company submitted such bids "not for the purpose of obtaining the business," but merely to remain on the bidder's lists (it is understood that a prospective bidder who continually declines to bid is dropped from the lists) and in this way to keep themselves informed as to potential needs for their products. The representative defended the trade practice of permitting the assembler to have the replacement parts business. One of the reasons given was:

It has always been recognized in our industry that the profit which our customers make on the spare parts that they handle is the thing that has been a large factor in keeping them in existence.

However, notwithstanding its belief that the assemblers should continue to get the replacement-parts business, Hercules has recently agreed to sell direct to the Government.

In testimony before the subcommittee, industry representatives took issue with various estimates contained in the staff memorandum with respect to packaging and other items of cost. The subcommittee does not propose to resolve the issues which were thus raised. Nor will the subcommittee attempt to say just what a reasonable price for any of these replacement parts would be. It is obvious, however, that in many instances the Government actually was gouged in the price paid, if not in the form of excessive profits then at least in the form of what might well be considered a disguised subsidy to certain segments of the automotive industry.

The Government is by far the largest single customer for automotive replacement parts. It is expected that in the stepped-up defense

program about a billion dollars a year may well be paid out in the parts program alone. The subcommittee feels strongly that the prices charged to the Government should be free of all economically unsupportable elements of cost. There is perceived no possible justification for paying a price which includes a duplication or triplication of the same service.

While it was unmistakably clear from the evidence presented to the subcommittee that certain trade practices did exist and that they were based upon long-standing customs or tacit understandings in the industry, there was evidence that in at least one instance a vehicle assembler exacted an express promise from a unit manufacturer not to compete for parts business. An official of the Federal Motor Truck Co., apparently dismayed that one of its suppliers, the Troy Sunshade Co., should submit to the Government a lower bid than Federal on a windshield made by Troy, called upon the supplier to quit bidding. In a letter to the chairman of this subcommittee, Troy Sunshade Co. stated that they do not quote the Government direct on windshield assemblies which they furnished to Federal, and added,

This does not represent a general policy of our company, but, as you are aware we made this agreement with Federal at their request.

PROCUREMENT PROCEDURES

Practically all of the procurement of automotive replacement parts is accomplished under the advertising for bids procedure. Traditionally, this method of procurement has been regarded as the best possible way for the Government to buy. It has been thought to afford all available sources the opportunity to secure Government business, and at the same time to insure to the Government a fair and reasonable price for the goods. However, the study of automotive parts procurement points up how injudicious administration of this procedure can completely nullify its advantages.

In the case of many of the parts being procured, there is little, if any, competition. This fact was known, of course, to the procurement officials of the Ordnance Corps and yet they continued to send out hundreds of invitations on items where they knew full well in advance that they would receive only one or two bids. They contended that they were forced to do this by reason of pressure from small-business groups and even congressional committees.

This subcommittee fully appreciates the importance of spreading Government business as widely as possible, and of giving the little fellow a chance to participate. However, this was not being accomplished under the policies and procedures being followed by Ordnance. For example, in many situations the invitation of bid specified a part manufactured by X company "or equal." The only blueprints of the part were in the possession either of the X company or its customer, a vehicle assembler. While invitations to bid were sent far and wide, it was impossible for anyone not in possession of the blueprints to bid on the part.

In preparing the invitations for bids there were included numerous items on the same invitation on the theory that this would reduce the paper work at the Tank Automotive Center. Many of the items thus included were not related or were not of the same general type, so that bidders were limited with respect to the items upon which they were able to bid. The invitations were sent to long lists of proposed bidders

on the theory that the greater the circulation, the more intense the competition would be. Actually, however, while the total number of bids received might give the impression of keen competition, there would be a number of items upon which only one or two bids would be received. As to these latter items, Ordnance officials should have realized that under the circumstances no real competition could be expected to exist. It would seem that a more careful segregation of the items included on invitations, together with action to remove the secrecy from the nature of the part inherent in the practice of referring to it on the invitation by the vehicle assembler's part number, would result in a sounder procedure for the procurement of parts.

Then there were situations where competition would exist, but only among vehicle assemblers. In other words, no matter what the low bid turned out to be, it necessarily had to include economically unsupportable items of expense. Little or no effort was made in such situations to go straight to the basic manufacturer of the part and attempt to buy from him at a price which would insure him a reasonable profit. It would seem that where the Government finds it essential to buy a proprietary article, negotiation is the only feasible method of procurement. This is best illustrated by the transactions with the Braden-Winch Co. This was one basic manufacturer who does bid on Government invitations covering parts manufactured by it. Naturally, however, when the specifications call for a Braden part, the company had no reason to expect effective competition with its bid on that part. Consequently, the prices charged to the Government for these parts appear to be excessively high. For example, one part which cost \$49.80 and which it sells to vehicle assemblers for \$84.70 was sold to the Government for \$84.50. It should be pointed out also that an examination of four transactions involving Braden parts sold to the Government discloses a total of 209 invitations to bid having issued with but 16 responses.

Another safeguard which is absolutely essential to any sound procurement procedure is a preaward survey. Basically, the purpose of this survey is to determine that the individual or concern submitting the lowest bid is financially stable and otherwise qualified to perform the work.

The subcommittee's staff found that little or no attempt had been made to ascertain the qualifications of the successful bidders in connection with the procurement of automotive parts. It was necessary for staff members to secure whatever information they did concerning the financial rating and equipment and plant facilities of the successful bidder by resorting to the individual contracts. However, in order to be effective, a central file should have been maintained on all information pertinent to each particular contractor. No contracts should have been awarded where the information was unfavorable or incomplete. As a minimum, such a file should have included information such as—

- (1) A physical check of the plant.
- (2) Credit rating information from recognized credit organizations.
- (3) A description of the organization of the contractor including a statement as to the ability and qualifications of his personnel.
- (4) A financial statement.
- (5) The type of business and method of operation.

Ordnance officials conceded that they had fallen down on the job of making preaward surveys. They excused this deficiency on the grounds that the stepped-up defense program imposed a burden far beyond their capacity to perform the work. They stated that any case of lack of preaward surveys was due to their determination to take a chance on the abilities of the low bidder rather than fail in getting the job done. They assured the committee at the hearings, however, that they have now finished the first phase of the program; have started tightening their procedures; adding to their staff, and polishing the operation to the degree of efficiency required.

It is significant, however, that in the experience of the subcommittee whenever an agency is forced to admit deficiencies or inefficiencies in their operations they are quick to point to a lack of sufficient personnel to do the work which has been assigned to that agency. The subcommittee staff in conjunction with personnel from the General Accounting Office actually visited the plants of many of the successful bidders and otherwise performed the various steps which should have been performed by Ordnance in connection with the making of preawards surveys. The work of performing such a survey is not so burdensome or time consuming as to justify the situation as it existed at the time of the subcommittee's study.

Another safeguard which should have been followed in connection with the award of contracts after formal advertising is the performance of a price analysis. It was found that in many cases there was attached to the contract a price analysis, but that it consisted solely of a comparison with a previous price paid for the same item. In view of the fact that excessive prices for automotive parts had been the rule rather than the exception for years, the value of such an analysis is questionable at best. A breakdown of the price into the various elements of cost and profit might have provided a reasonable analysis. Only if these elements of cost were economically supportable and only if a reasonable profit had been included in the price could a proper determination be made that the bid was an acceptable one to the Government.

Basically, however, the real trouble lay in the fact that the procurement officials at the OTAC had for years been following a blind path, thinking that they were powerless to do other than advertise for bids and accept the lowest bid. They should have known, if in fact they did not, that the advertising method is sound only if judiciously employed.

CONCURRENT SPARE PARTS

Thus far this report has spoken only of replacement parts. However, it is commonly recognized that there are two separate phases of the automotive-parts program: that involving the procurement of replacement parts and the procurement of what is known as concurrent spare parts. "Concurrent spare parts" is a term applied to certain quantities of parts purchased concurrently with the vehicle. The quantities and types purchased are based upon an estimate on what will be needed to maintain the vehicle for the first 21 months of the life of the vehicle. These concurrent spare parts are procured from the vehicle assemblers in all cases and are, in fact, covered by the contract under which the vehicles themselves are purchased. Naturally, of course, all that has been said about the extra items of ex-

pense in connection with the procurement of replenishment parts applies to the procurement of concurrent spare parts. However, the subcommittee found that while Ordnance officials agreed in general with the contention that there are unjustifiable elements of cost included in prices paid for replacement parts, they defended vigorously the policy of buying concurrent spare parts from the vehicle assemblers and paying the higher prices.

Army officials put forth various reasons for their contention that the policy of buying concurrent spare parts is sound. Also, they stated that on the several occasions when they departed from this policy there was a breakdown in the field of the vehicles due to a lack of parts to maintain them. Accordingly, they feel that the advantages which they secure are more than offset by the added expense to which they are put in buying them from the vehicle assemblers. There were three or four reasons given which impressed the subcommittee: In the first place it was contended that this policy obtains only with respect to military vehicles and that these vehicles are constantly being redesigned and improved. Accordingly, even after the original vehicles are built there ensues a number of engineering changes. These engineering changes require different spare parts, and for maximum flexibility the concurrent spare parts orders necessarily must conform almost automatically to the changes which are made in the vehicle.

The Army also contended that they are fearful that if they have to obtain the parts separate from the vehicle they might be faced with a situation where they would have the vehicles delivered but would be unable to secure the spare parts. Recently, they have included in their contracts for the vehicles a provision under which they can refuse to accept delivery of the vehicles unless the concurrent spare parts are delivered also. Another reason which seemed to be sound involved the question of contract administration. It was contended that to procure the number of spare parts necessary requires thousands of individual contracts with consequent administrative expense. This expense is kept to a minimum where the provision for concurrent spare parts is included in the one contract covering the delivery of the vehicles.

The subcommittee has no basis upon which to appraise the soundness of these reasons of military necessity and therefore cannot recommend discontinuance of the existing policy of procuring concurrent spare parts. This is not to say, however, that the program as it has been administered in the past should continue without improvement. There are various aspects to the procurement of concurrent spare parts which are very disturbing to the subcommittee and upon which corrective action immediately should be taken.

For example, there have been occasions in the past when items such as tires, tubes, and batteries have been included in the parts to be furnished concurrently with the vehicles. Ordnance apparently realizes that there is no justification whatever for buying these items from the vehicle assembler. There are indications that steps have been taken rather recently to eliminate such items from the list of concurrent parts. This policy should be strictly enforced.

Moreover, there are items which are commonly referred to as standard hardware items which need not be procured from the vehicle assembler. Care should be taken by Ordnance officials to see that future

contracts, including the delivery of concurrent spare parts, are carefully reviewed to insure that there are not included among the items any parts which might better be procured directly from the basic manufacturers.

Another phase of this same subject which gives the subcommittee concern is the practice of buying parts concurrently where there is already in stock a sufficient quantity to satisfy the needs for years to come. The subcommittee found some evidence that there were being included as concurrent spare parts, items which were already on hand sufficient in number to last anywhere from 1 to 104 years based upon the highest annual need for such items. Ordnance officials attempted to justify this on the grounds that they adopted a policy about the time of the outbreak of the Korean war of buying all parts without regard to their existing supplies merely as a temporary expedient necessitated by a lack of time to check their inventories. Whether this be the reason or not, the subcommittee is interested only that in the future a careful screening of existing supplies be made in connection with the approval of items for inclusion as concurrent spare parts.

Another aspect of the concurrent spare-parts program which appears to warrant careful consideration and appropriate action is the price being paid by the Government for such parts. The subcommittee was surprised to find that in many cases the Government was paying a higher price for a part purchased concurrently with the vehicle than it was paying to the same supplier for the same item when it was purchased as a replacement part. The testimony at the hearings was to the effect that concurrent parts actually should be priced lower than replacement parts. This was admitted even by the vehicle assemblers themselves. Consequently, the subcommittee urges strongly upon the Ordnance Corps that strenuous steps be taken to review future prices being paid for concurrent spare parts.

In this connection, reference was continually made by Ordnance officials to the fact that these contracts covering the delivery of vehicles and concurrent spare parts contained a price-redetermination clause and that as yet there have been no redeterminations of the prices referred to in the staff study which were in excess of the prices paid for replacement parts. The subcommittee is pleased to know that these contracts do contain a provision which could, if properly administered, protect the Government's interest in this respect. At the same time, there was some indication that too much reliance is being placed by Ordnance officials with respect to price-redetermination clauses. As in the case of renegotiation, a price-redetermination clause is no substitute for sound pricing in the original contract. Every effort should be made to fix a fair and reasonable price in the original contract and not resort to slipshod or haphazard methods of price fixing, hoping that any excess will be recovered in connection with the price redetermination.

There is one final aspect of this concurrent spare parts program which also should be carefully watched. It apparently is the practice for the vehicle assemblers to designate which parts should be furnished as concurrent spare parts. Ordnance officials stated that it was their function to review this list of concurrent spare parts as prepared by the assembler and approve it. This practice, while supposedly the only sound approach, is naturally subject to abuse. There should be a careful and skillful screening of the particular items to be furnished in order that it will be kept to a minimum and will include only those

parts which for reasons of military necessity and administrative efficiency should be included in the vehicle contract.

MANUFACTURERS' AGENTS AND MIDDLEMEN

As previously indicated, the staff of the subcommittee also looked into the question of the financial standing and qualifications of the successful bidders in some cases. It was found that many small business firms seeking to do business with the Government found it necessary to employ manufacturers' agents on a percentage or even full-time basis to represent them at the Tank Automotive Center. There was testimony from several of these small firms and also from the agents themselves, the substance of which was that by reason of the complicated contracting procedures and forms employed by the Government a small business firm would be foolish to try to do business with the Government without the services of someone who knew these procedures and was familiar with the content of the forms.

The subcommittee gathered the impression that this practice is not confined to a few small companies but is rather widespread, particularly in the Detroit area. Strangely enough, as has also been brought out in this report, the procurement method has been largely the formal advertising-for-bids procedure. It would seem that a system which enables a low bidder to include in his price 5 percent or more to cover the services of a manufacturer's agent and still secure the contract must be faulty in some respects. Heretofore, 5-percenters have associated themselves primarily with negotiated contracts. In this field they have relied upon their influence, proper or improper, to secure Government business. However, in the majority of cases examined by the subcommittee during its hearings the 5-percenters secured their commissions on contracts awarded after advertising.

One particular manufacturer's agent who seemed to typify the type of individual and organization which seems to be rather widespread in Detroit was Mr. Arthur Higginbottom, doing business under the name of Art Higginbottom Associates. He testified that he represented, on a commission basis, four small companies, each of which was producing entirely different items. The company's location, products and estimated number of employees as testified to by Mr. Higginbottom were as follows:

(a) Industrial, Experimental & Manufacturing Co., Detroit, Mich., a sheet metal manufacturing company employing 15 people.

(b) Keeler Machine Co., Detroit, Mich.; a machine shop employing 25 people.

(c) Squires Gauge Co., Berkley, Mich.; a gage manufacturer employing 10 people.

(d) Peerless Gear & Machine Co., Toledo, Ohio; a small manufacturing company employing 40 people.

Mr. Higginbottom stated that he watched the bid invitations for the type of item which one of these companies could produce with its existing facilities. When he located an item he would return to the company, secure from them a price estimate—which naturally would include his commission—and then he would assist the company in preparing the appropriate bid forms. He would attend the bid openings and supply the necessary liaison work with Ordnance until the items were delivered. Mr. Higginbottom appeared to the sub-

committee to be a sincere, conscientious man who knew his end of the business and whose experience ably equipped him to represent these companies in an honorable and satisfactory manner. In fact, this type of situation has all the outward appearances of one which is not disadvantageous to the Government.

In another situation, it was found that the Macomb Auto Supply, Inc., could afford to carry on its payroll two men at \$10,000 per year each, plus expenses, subcontract all its work and still make a profit. Macomb was just an automotive-parts stockroom and had no facilities for the manufacture of parts under Ordnance contracts. One of the two men employed by Macomb to secure Government business was a former Ordnance inspector, although prior to the employment of this ex-former inspector, Macomb had very little Government business. During the period of 18 months immediately ensuing his employment, Macomb obtained 13 contracts totaling over \$300,000. These contracts were administered by the two new employees from their desks in the office of another company. The work was entirely sublet and even the packaging was done by a firm other than Macomb. The former Ordnance inspector had an arrangement with a packaging firm whereby he would secure a commission also on work which was subcontracted to that firm. The fact that such commissions and salaries can be paid out leads inevitably to the conclusion that there is inherent in the prices for many of these contracts a large chunk of fat.

Another case involved the Metro Engineering & Manufacturing Co. John J. O'Haire, a captain assigned to the office of the Chief of Ordnance, went into the Inactive Reserve in August 1946. He remained in the same office as a civilian until May 1947, when he resigned and went to Detroit, Mich. He and his brother, James P. O'Haire, a part-time accountant for the Metro Engineering & Manufacturing Co., formed the partnership of O'Haire & O'Haire, procurement specialists and industrial consultants. Neither of the O'Haires had any previous background in manufacturing and sales, both being accountants by profession.

On June 3, 1947, the Metro Engineering & Manufacturing Co. and the O'Haire partnership signed a contract providing that the O'Haires would solicit Government orders for the services and products of Metro for 10 percent of the gross dollar amount of each order accepted. On March 1, 1948, the commission was reduced from 10 to 5 percent plus \$6,000 per year to act as financial advisers to Metro. On January 3, 1949, the fee for financial advice was changed to one-half of 1 percent of gross billings to the Government. On January 2, 1951, the contract was amended to provide total payment of \$24,000 in 1951 for services, both as to sales and financial advice.

Government sales and amounts paid to the O'Haires from the inception of the contract to December 31, 1950, were as follows:

Year	Commercial sales	Government sales	Paid to O'Haire & O'Haire
1947.....	\$159,718.38	\$377,151.80	\$37,715.18
1948.....	82,905.95	409,340.69	29,924.86
1949.....	34,289.31	787,372.49	38,768.11
1950.....	151,056.62	706,551.64	45,191.54
Total.....	427,970.26	2,280,416.62	148,599.69

Sales expenses, consisting of entertainment, travel, and gifts, of Metro for the same period were as follows:

1947-----	\$1,273.48
1948-----	20,362.95
1949-----	22,458.51
1950-----	15,612.43
Total-----	59,707.37

Sales expense of O'Haire & O'Haire for the same period is as follows:

Year (June 1 to May 31)-----	
1948-----	\$18,206.81
1949-----	21,424.04
1950-----	21,342.01
1951 (to Apr. 7, 1951)-----	9,452.32
Total-----	70,425.18

On one contract for \$182,750, that was subcontracted in its entirety, Metro realized a gross profit of \$50,602.28. The O'Haire brothers, both accountants by profession, in testimony before the subcommittee claimed a net profit of \$19,625.63, computed as follows:

Sales price-----	\$182,750.00
Direct costs-----	133,931.20
Material, handling, and hauling-----	6,696.55
Administrative expense, at 9½ percent of cost-----	13,359.62
Commission to O'Haire & O'Haire-----	9,137.00
Total-----	163,124.37
Net profit-----	19,625.63

Under questioning it was admitted that the only indirect labor account on their books totaled \$10,270.84. This consisted of the time of two janitors and some idle time of employees incurred while attending a Christmas party. It was from this account that they allocated the \$6,696.55 for material handling on the contract in question as shown above. The commission figure, of course, speaks for itself. As to the claim for administrative expense of 9½ percent, the administrative expense of Metro for 3 years included \$35,421.32 for entertainment and \$19,970.78 for gifts and miscellaneous.

Under questioning it was admitted that the company's expense accounts mentioned above contained numerous articles, such as television sets, watches, hunting equipment, cameras, clothing, and a stuffed bobcat, that were personal items bought for its officers. In addition, the expense of putting in a recreation room in the home of one of their own officers was also charged as company expense.

The subcommittee agrees with the strong denunciation of such outfits by its chairman * * * during the hearings when he stated:

But to the extent that they do not perform any economic service, they are parasites in my book.

The subcommittee feels that Ordnance should make every effort to avoid doing business with this type of organization. One of the ways in which this can be accomplished is to make a thorough investigation wherever it appears that the bidder has employed a commission agent in connection with the award of the contract. This brings us to a problem which was pointed up in testimony by several of the manufacturers' agents.

On the bid form there is a question which the bidder is required to answer which reads as follows:

The bidder represents that he has or has not employed or retained a company or person other than a full-time employee to solicit or secure this contract, and agrees to furnish information relating thereto as requested by the contracting officer.

The bidder is required to check in the proper space as to whether he has or has not employed such a person. There was considerable testimony that a manufacturer's agent who worked on a 5-percent basis for several companies could be regarded as working full time for each company. While this interpretation is unreasonable and certainly not in accordance with the intent and purpose of the language, the fact remains that it has been so interpreted. Mr. Higginbottom testified that he was working full time for four different companies. Another agent maintained that he was working full time for 11 different companies. Under such circumstances it seems imperative that the language of this particular provision be revised so that it cannot be misinterpreted and so that it will not fail.

CONCLUSION

For many years automotive-parts manufacturers have refrained from competing with vehicle assemblers in the sale of replacement parts to the Government. These trade practices have increased by untold millions of dollars the cost to the Government of procuring automotive parts. While both segments of the industry—unit manufacturers and assemblers—defend this practice as being economically sound and advantageous to the Government, this subcommittee could find no justifiable basis, as a general proposition, for buying replenishment parts from other than the source manufacturer.

Until the time the subcommittee began its investigation, the Ordnance Corps of the Army had supinely accepted as beyond their control the existence of these trade practices and the obviously excessive prices being paid for parts. The action thus far taken by procurement officials in attempting to deal directly with the manufacturing source is a step in the right direction. However, forceful measures must continuously be adopted. The only way to cope with a condition as deep-rooted as this one is to fight strength with strength. The Government is not without the power to eliminate these trade practices if a sincere and intelligent effort is made to do so.

In addition, deficiencies in the procedures for the procurement of automotive parts have created an opportunity for middlemen of all kinds to insert themselves and thus add unnecessarily to the cost of the defense program. Ordnance officials apparently relied on the advertising for bids method of buying as a sure-fire guaranty of fair and equitable prices. However, under the conditions found by the subcommittee to exist, unjudicious use of these procurement procedures had resulted in the payment of prices which had been inflated beyond all reason by repetitive costs and pyramided profits.

RECOMMENDATIONS

(a) The Department of the Army

(1) Ordnance should strenuously pursue the principles and procedures set forth in the directive of August 17, 1951, from the Chief of Ordnance relating to the direct purchase of replacement parts.

(2) Where companies are found to adhere to trade practices which unnecessarily add to the cost of parts procurement, consideration should be given to the feasibility of procuring, in the first instance, vehicles which will not include such parts.

(3) Consideration should be given to the possibility of negotiated contracts where no real competition is found to exist.

(4) In the preparation of invitations to bid an effort should be made to include only items of the same or similar nature.

(5) There should be maintained a central file containing full and accurate information concerning every individual or organization doing business with the Tank Automotive Center.

(6) The provision in the bid form designed to disclose the presence of 5-percenters should be revised to eliminate any possibility of misinterpretation.

(7) An effort should be made to correct the situation where the lack of available blueprints, or reference to an item merely by the vehicle assembler's part number, has stifled competition.

(8) The procedure under which bids submitted on an "or equal" basis are evaluated should be carefully reexamined with a view to determining whether the standards being applied are excessively rigid.

(9) Establishment of bid analysis procedures which will insure that no more than a fair and reasonable price is being paid even where let on an advertised bid basis.

(10) More care should be taken in the procurement of concurrent spare parts with respect to the elimination of—

(a) Items such as tires, tubes, and batteries;

(b) Standard hardware items;

(c) Parts already in adequate supply;

(d) Parts known to be interchangeable;

(e) Parts not justified by considerations of military expediency.

(11) Effort should be made to eliminate all those who contribute no economic service to the sale of automotive parts to the Government.

(b) Federal Trade Commission

(1) A thorough study should be made of the legality of the trade practices found by the subcommittee to exist in the automobile industry. Appropriate proceedings should be instituted if warranted.

(2) Existing laws should be studied with a view to determining whether loopholes exist which in the public interest should be closed. If so, appropriate legislative changes should be suggested to the Congress.

(c) General Services Administration

The contents of this report should be carefully considered and pertinent recommendations followed in connection with the procurement of automotive parts for civilian agencies of the Government.

